



SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1941

No. 1274

W. E. RICHARDSON, TRUSTEE, ETC., ET ALs.,
Petitioners,
vs.

BLUE GRASS MINING COMPANY, ET ALs.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF
CERTIORARI.

I.

Opinion of Lower Court.

The Circuit Court of Appeals wrote no opinion in the case, but merely entered a decree (R. VI, p. 2183), reciting that, for the reasons set forth in the opinion of the District Court, the cause, on both respondents' original appeal and petitioners' cross-appeal, was affirmed. The opinion of the District Court is published (29 Fed. Supp. 658), and will be found in the record, Vol. I, p. 358. The Court of Appeals affirmed without opinion.

II.

Findings of Fact in the Lower Courts Relied Upon.

The findings of fact and conclusions of law by the District Court, affirmed in the Court of Appeals, will be found in the Record, Vol. I, at pp. 385-417.

III.

Statement of the Case.

We adopt the statement contained in the petition for certiorari, though some additional facts may be brought to the attention of the Court in brief and argument.

IV.

Probable Errors and Questions Presented.

The probable errors and questions presented for decision are fully set out in the petition for certiorari and need not be repeated.

V.

Jurisdiction.

We rely upon the Act of March 3, 1891, 26 Stat. 828, as amended and codified in U. S. C. A., Title 28, Sec. 347, and Rule 38 of this Court, especially Section 5, sub-section (b) thereof, which provides for allowance of the writ.

"Where a Circuit Court of Appeals has rendered a decision in conflict with another Circuit Court of Appeals on the same matter, or has decided an important question of local law in a way probably in conflict with applicable local decisions * * * *".

It is submitted that the Circuit Court of Appeals, Sixth Circuit, has rendered a decision:

- (1) Probably in conflict with the decisions of other Circuits and of this Court;
- (2) of an important question of local law probably in conflict with applicable local decisions, and
- (3) On an important question of general law in a way probably untenable and in conflict with the weight of authority.

IV.

BRIEF AND ARGUMENT.

By applicable decisions of Kentucky, as well as by the weight of authority of other circuits and of this Court, trustees guilty of wilful fraudulent breach of trust, and who denounce their trust and seek to appropriate the trust estate to themselves, should be denied all compensation for services.

In *Erie Railroad v. Tompkins*, 304 U. S. 64, this Court held that, except in matters governed by the Federal Constitution or by acts of Congress, the law to be applied in any case is the law of the State, whether it be declared by legislative enactment or by its highest court in a decision.

304 U. S. 78.

The case at bar is of such local character. The corporations of which respondents were officers and directors, were Kentucky corporations; their properties were situated and their business transacted, in Kentucky; the contracts upon which petitioners' rights rest, were to be performed in Kentucky; the trust was being administered by respondents in Kentucky, and the cause of action arose there. Federal jurisdiction rests alone upon diversity of citizenship. The controlling law and public policy of Kentucky has been announced by the highest court of that State.

Cominger v. Louisville Trust Co., 128 Ky. 697, 108 S. W. 950, 111 S. W. 681, 129 Am. St. Rep. 322.

We submit this case declares the law of Kentucky to be that "a trustee guilty of fraud or misconduct in the management of the estate is not entitled to compensation", certainly if such misconduct is found as it was in the case at bar, to be grounded in bad faith.

Again in *Weakly v. Meriweather*, 156 Ky. 304, 160 S. W. 1054, the rule was applied, though the trustee was not convicted of bad faith. The Court in the latter case, however, might have been influenced by the fact that little service was rendered by the trustee, who had commingled trust funds with his own, other than payment of interest.

The common law of Virginia, from whose territory the State of Kentucky was carved, seems to have been declared to the same effect.

Boyd v. Boyd, 3 Grath, 113;

Ward v. Funston, 86 Va. 359, 10 S. E. 415.

This latter may not be material, except insofar as it discloses a settled policy of these people of a common stock who at one time acknowledged a common independent sovereignty.

But if the question be treated as one of general law, rather than one of local law, the decision below is probably untenable and contrary to the weight of authority, including decisions of this Court and the Courts of other circuits.

Walker v. Beal, 9 Wall. 743, 19 L. Ed. 814-20;

Barney v. Saunders, et al., 16 Howard 535, 14 L. Ed. 1047, 1050;

Wadsworth v. Adams, 138 U. S. 380, 34 L. Ed. 984;

Lewis v. Ingram (C. C. A. 10th), 57 F. (2d) 463-465, certiorari denied 287 U. S. 614, 77 L. Ed. 533;

Munro v. Smith (C. C. A. 1st), 259 Fed. 1;

Flint River Pecan Co. v. Fry (C. C. A. 5th), 39 F. (2d) 457;

Backus v. Finklestein (C. D. Minn.), 23 F. (2d) 357, appeal discontinued by stipulation 31 F. (2d) 1011;

In Re Polansky (D. C. S. D. N. Y.), 41 F. (2d) 547;

Caldwell v. Hicks (D. C. S. D. Ga.), 15 Fed. Supp. 46; *Davis v. Swedish Am. Nat. Bank*, 78 Minn. 408, 80 N. W. 953, 81 N. W. 210, 79 A. S. R. 400;

In Re Hedges Estate, 66 Vermont 70, 44 A. S. R. 820; *In Re Kline*, 280 Pa. St. 41, 124 Atl. 280, 32 A. L. R. 926; *Turner v. Ryan (Iowa)*, 272 N. Co. 60, 110 A. L. R. 554, and note at p. 572.

In the Restatement of the Law of Trusts, Sec. 243, subsec. d, the rule is thus succinctly stated:

“If the trustee *repudiates* the trust or misappropriates the trust property or if he *intentionally* or negligently mismanages the whole trust, he will ordinarily be allowed no compensation.” (Italics ours.)

The District Court found, and the Circuit Court of Appeals concurred therein:

(1) The Kentucky group “attempted to appropriate all of the stock to themselves, without notice to the Tennessee Group. In numerous other ways they revealed a deliberate design to deprive their Tennessee associates of all beneficial interest in the corporations.”

Opinion 29 Fed. Supp. 664;

Finding of facts (23) R. I., p. 391.

(2) That they engaged in various specific instances of misconduct, and in “various other questionable transactions in connection with the business, all without the knowledge of or notice to the Tennessee Group”.

Finding of facts (21) R. I., pp. 390-391.

(3) That their use of trust funds to promote their own interests, “was clearly wrong and indefensible”.

Finding (44) R. I., pp. 399-400.

(4) That they were guilty of “fraudulent breach of trust”.

Conclusion (20) R. I., p. 416.

We cite some of the instances making up the “fraudulent breach of trust” found by the Courts below:

Reference has already been made to the deliberate attempt of the Kentucky group at the organization meetings to appropriate to themselves all of the stock of both corporations (R. VI, pp. 1812-18), and this at a time when Mr. Johnson concedes the Tennessee Group were entitled to equal ownership of the stock (R. III, p. 790, Qs. 620-21). In the face of this action, Mr. Johnson, Sr., wrote Messrs. Powell and McArthur, of the Tennessee Group, advising them that the organization meetings had been held and requesting that they put up their part of the agreed working capital (R. II, pp. 80-81). The Tennessee group were not advised of this action and did not know of it until near the close of the trial below, when Mr. Johnson produced some minutes which were written up after this suit started (R. VI, pp. 1820-24). Johnson, Sr., was asked why he did not invite Richardson and Garth to attend the organization meetings, the latter of whom was on the ground, to which he replied he thought the Tennessee group were to pay for their stock only if the first sale was confirmed on appeal. Thereupon the Court reminded him this action was taken before the reversal of the first sale (R. III, pp. 817-20). This excuse is clearly a specious one. If it were not intended that the Tennessee group should take and pay for one-half of the stock, why did the parties go to the trouble of having them subscribe for one-half?

The Kentucky group appropriated to themselves large salaries, the first year of the operation of the business, to-wit: the year 1930, aggregating the sum of \$34,100.00 (Bl. Grass Min. Co. Aud. p. 35, and Pendleton Store Audit, p. 39).

The only statements ever rendered to the Tennessee group for January, February and March, 1930 (R. II, pp. 410-43 and R. III, 433-446), showed no salaries to proprietors or executives but Pendleton Store statements did show

a payment to J. E. Johnson, Jr., of \$50.00 for legal services, and salary of Arch Pendleton of \$150.00 (R. II, p. 425) and a payment to "Wm. Pendleton of \$150.00 (salary for January, Feb. and March)", (See R. III, p. 434). These statements were false. The minutes of the meeting of January 15, 1930, showed the directors had fixed the salaries for Pendleton Store for Wm. Pendleton at \$2,400.00 for 1930; for Arch Pendleton at \$5,000.00, and for J. E. Johnson, Jr., at \$2,400.00 "Said salary to be in lieu of all other fees" (R. VI, pp. 1819-20). As a matter of fact the minute entry was false, as well as the entry on the books of account at July 31, 1930, setting up salaries for the Kentucky group and charging them with stock subscriptions, because the witnesses testified no salaries were agreed upon or fixed until November or later in 1930 (R. III, pp. 661-2; 681-2; 810-12).

The day after Mr. Johnson had by false representations induced Richardson, Trustee to sign the alleged contract of February 18, 1931, putting as he evidently thought, the Tennessee group in the position of minority stockholders, he began having Blue Grass lend money to Black Gold Mining Company (they had already furnished labor and credit (R. IV, pp. 1414-15)), the first loan being February 19, 1931, and kept it up until the total loans and advancements aggregated \$22,242.31. (Ex. X Lavinder.) Mr. Johnson very distinctly recalled no loans were made until after the alleged contract of February 18, 1931 (R. V, p. 1640). Less than three months before these loans started Mr. Johnson had written Mr. McArthur that the Blue Grass was having a hard time to get money to meet its pay roll (R. II, p. 355). In August, 1931, Johnson began lending the corporate funds to the aggregate of \$4,302.15, to Chavies Coal Co. (Ex. X Lavinder), a Johnson company organized by him to take over one which he had operated to bankruptcy (R. V, pp. 1702-4). And in August, 1931, he caused Blue

Grass Mining Company to lend \$1,000.00 to Johnson Supply Company and to buy its stock certificate book for \$5.25 (Ex. X Lavinder). This was a Johnson Company (R. V, pp. 1700-01). In November, 1933, Johnson caused corporate funds to be loaned to Eagle Coal Company in the sum of \$816.00 (Ex. X Lavinder) which was owned by Johnson, Pendleton and Davis (R. V, p. 1701). In 1934 he loaned corporate funds to Sun Fire Coal Company to the extent of \$7,750.00 (R. IV, pp. 912-18), this latter company being owned by J. E. Johnson, Jr., Wm. Pendleton and Arch Pendleton (R. V, p. 1701). These loans were subsequently repaid. No interest was paid on any of these loans, except a small amount on a part of the Black Gold loan.

The ink was scarcely dry on the Sun Fire loan when Pendleton and Joe Johnson, Jr., in response to an urgent appeal from Mr. Powell who was sick and needed help, wrote Mr. Powell that Blue Grass Mining Company was hard up, could not keep enough money to run the business and had to borrow to meet expenses (R. IV, pp. 902-4).

Although it appears by pleadings sworn to by Mr. Johnson, and orders entered in suits involving the properties that the properties were bid in at the second sale by Johnson, Jr., for the use and benefit of Blue Grass Mining Company (R. V, pp. 1673-78; 1688-92; 1694-99) and admitted by Johnson, Sr., that it was bought at the second sale for Blue Grass Mining Company (R. III, p. 728; R. III, p. 791), Johnson, Jr., insisted he bought it for himself and father (R. IV, p. 959), and they set up royalties on books of the Blue Grass Mining Company of nearly Forty Thousand Dollars (R. V, p. 1534; R. III, pp. 699-703).

Johnson, Sr., used \$9,020.00 of Blue Grass funds in 1935 to buy a tract of coal land needed by the Company, known as the Crawford tract. However, he took title in his own name, later borrowed money on a note to be paid out of royalties to repay the Mining Company, leased the land to

the Mining Company and at the time of this suit had drawn \$12,245.00 in royalties (R. III, p. 610; R. V, p. 1416; R. III, pp. 851-56), (Decree Sec. VII, R. I, pp. 422-23). We particularly invite the Court to read Mr. Johnson's testimony regarding this transaction, under questioning by the District Judge beginning at Record III, p. 852, as illustrating his callousness toward his obligations as a trustee. He insisted upon holding this land until ordered in the case to convey it to the Mining Company.

The Baker tract was purchased by Wm. Pendleton for \$600.00, leased by him to Blue Grass by whom it was needed, and from which the royalties drawn by Mr. Pendleton and the Johnsons amounted to over six thousand dollars (R. IV, pp. 928-35; R. V, pp. 1415-16; R. I, p. 395; R. III, p. 611; R. V, p. 1415; Decree Sec. VIII, R. I, pp. 424-5).

The Kentucky group organized a sales company with funds of Blue Grass Mining Company and claimed the stock in their own names and insisted upon such claim until the Court decreed ownership to Blue Grass Mining Company in this case (R. VI, pp. 1749-53; R. I, p. 425).

The Kentucky group employed numerous members of their families and not only paid them salaries but paid and set up large bonuses for them, which the Court was compelled to order paid back or cancelled (R. I, pp. 400-01; R. VI, pp. 2070-98; Decree XIV, R. I, p. 427).

The Kentucky group always led the Tennessee group to believe the companies were making no money and were hard up (R. II, pp. 206-7; 333; Ex. 11, R. II, p. 344; Ex. 17, R. II, pp. 355-56; p. 547; R. IV, pp. 901-5; R. IV, p. 912; R. IV, p. 917). Notwithstanding these representations they were lending Blue Grass money to themselves and their other corporations in sums aggregating in excess of \$40,000.00, and drew out of the two corporations in cash, from 1930 until this suit was tried \$166,655.07 in salaries (R. I, pp. 405-6; R. VI, pp. 1983-89), and from Black Gold, financed

largely or altogether by Blue Grass funds, over \$50,000.00 (R. I, p. 407), and in 1936, while this suit was pending they declared to themselves a 100% dividend on all stock of Pendleton Store, Inc., and a 50% dividend on all the stock of Blue Grass Mining Company, to the exclusion of petitioners (R. I, p. 393). They made all sorts of false entries upon the books (R. IV, pp. 1156-58; 1163-68; 1173-74; 1189; 1193-94; 1211-12; 1262; R. V, pp. 1501-04; 1550-51; 1518-22; 1760, 1810).

They engaged in other questionable transactions too numerous and some too petty to annoy the Court with, such as payment of the license for a privately operated tavern; withdrawal of \$5000.00 from the insurance or Workmen's Compensation fund. Finally, after having treated and dealt with complainants as co-stockholders and co-adventurers for about seven years, they come into Court and denounce their trust, deny complainants have any rights or interest, and assert that the \$2500.00, one-half of agreed working capital called for by Mr. Johnson (Powell Ex. 2, R. II, pp. 80-81), and promptly put up by complainants (R. II, pp. 9; 45; 82-3), was not working capital at all but was advanced as a loan (Amended Ans. R. I, p. 213). Indeed their bookkeeper and witness Simpson, said it was a gift (R. V, p. 1535).

This claim was so utterly unfounded as to border upon the ridiculous and very properly received scant attention by the Trial Court (R. I, pp. 364, 366, 387). The Kentucky group never did put up their one-half the working capital, though Mr. Johnson did advance \$1495.00 in opening the mine which he charged to expenses and got back in 1930 (R. VI, p. 2056), and this \$2500.00 was all the actual invested capital ever put into the two companies. In the face of this fact, and of their own failure to put up their share of the capital, Johnson, Sr., swore in this case that \$5000.00 capital was wholly inadequate (R. III, p. 649). But on cross-

examination he admitted that this \$2500.00 was all the money put into the corporations and had resulted in earning about \$80,000.00 (this was after the auditor threw back into earnings royalties set up), and had paid executive salaries in excess of \$150,000.00 (R. III, pp. 713-32, Q. 389).

We thus find a wilful, premeditated fraud running through all of the dealings of these members of the Kentucky group with the corporations and with their co-stockholders, the members of the Tennessee group. We know of no case where trustees who have been guilty of such a consistent course of misconduct have been allowed compensation for their services. We respectfully submit the case of *Pierce v. Dahlgren*, 300 Fed. 268 (C. C. A. 6th) cited by the Honorable District Judge does not support his allowance of compensation. In that case, the Circuit Court of Appeals, Sixth Circuit, speaking through Judge Denison, before allowing the Trustee's salary, was at great pains to discover whether she was acting in good or bad faith in her dereliction of duty in making a loan to herself secured by a pledge of her interest in the estate. The care with which Judge Denison went into the question of good faith strongly indicates his decision would have been otherwise if the misconduct had been wilful and in bad faith. Judge Denison cited in support of the decision of the court in the Pierce case, the case of *Garesche v. Levering Co.*, 146 Mo. 436, 48 S. W. 653, 46 L. R. A. 232. An examination of this last case reveals that the good faith of the trustee was made the touchstone for the allowance of compensation. The same is true of *Paducah Land &c. Co. v. Hayes*, 15 Ky., L. R. 517, 24 S. W. 237, likewise cited by the learned District Judge in support of his opinion. In this latter case the Court held the trustee, President of the corporation, had accounted for all stock sold, and as to stock not sold, but held by him, he was liable for its value rather than for the price at which he might have sold it, "as his was not a wrongful conver-

sion". Thus he was acquitted of any fraud or intentional wrong, and nothing other than mistake of judgment stood in the way of allowance of compensation. Nor do we believe the other authorities cited, that is, 65 C. J., p. 929, Sec. 840 (R. I, p. 377), afford support for the opinion under the facts of the case at bar. In fact that section opens with a statement of the general rule that a trustee who neglects his duties, or is guilty of bad faith, or violates his obligations, "*or who repudiates the trust, claiming title as absolute owner,*" forfeits his compensation. (Italics ours.) The section then states the exceptions to the general rule, but we submit the case does not come within the exceptions. On the contrary in the case at bar the trustees violated their obligations, were guilty of bad faith, repudiated the trust, and claimed the title as absolute owners.

Flint River Pecan Co. v. Fry, supra, and *Backus v. Finklestein, supra*, in both of which compensation was denied, are nearly parallel in their facts to the case at bar.

The record in this cause will disclose that the respondents worked primarily at all times for their own benefit, and only incidentally for the benefit of the corporations of which they were officers and directors. Compensation should be the reward of faithful and honest service, and never of unfaithful self-service, especially where the trust estate and beneficiaries have been by the trustees put to an enormous expense as in this case, to establish the trust and bring the trustees to account.

V.

The opinion and decree of the courts below permitting the respondent trustees to hold the stock of Black Gold Mining Company are probably contrary to the decisions of this Court, the courts of other circuits including the Sixth Circuit, and to the weight of authority.

The facts with reference to the organization by members of the Kentucky group of Black Gold Mining Company, as

found by the Trial Court and concurred in by the Circuit Court of Appeals (Finding of Facts No. 44), will be found at pages 399-400, Volume I of the printed record. Stated in little more detail, they are as follows:

Black Gold Mining Company was organized by members of the Kentucky group with whom is also associated W. E. Davis, the Receiver in the State Court proceeding, from whom the Blue Grass properties had been purchased, and one H. K. English, a coal operator of repute in that section of Kentucky (R. III, p. 660). English put no money into the business and soon sold out what interest he may have had to Johnson, Sr., a member of the Kentucky group (R. III, p. 721). William Pendleton and J. E. Johnson, Jr., were or became interested (R. III, pp. 841 and 868). No stock was ever issued, but the stockholders at the time of the trial of this case were W. E. Davis, \$1667.00; William Pendleton \$1667.00; J. E. Johnson, Jr., \$1666.00, and the stockholders of Jeda Coal Company, which is only a holding company, were J. E. Johnson, Sr., J. E. Johnson, Jr., Wm. Pendleton, all members of the Kentucky group, and E. J. Davis and W. E. Davis. The stock, according to the books was paid for by setting up salaries and charging those salaries with stock subscriptions (R. V, pp. 1654-55).

On December 12, 1930, Hazard Coal Corporation, which owned the property subsequently acquired by Jeda and Black Gold, entered into a contract with Johnson, Sr., and H. K. English agreeing to lease to Johnson, English and W. E. Davis, the properties known as the Ashless properties, and permitting them to transfer it to a corporation of \$25,000.00 paid in capital, or to make the lease direct to the corporation and to lend to them \$10,000.00 to be repaid in installments equal to 5¢ per ton on coal mined from the properties (R. VI, p. 1756). Davis did not sign the contract but agreed to be bound (R. VI, pp. 1756-57). The lease was subsequently executed by the Hazard Coal

Corporation direct to Jeda, which Company was to pay its lessor 10¢ per ton royalty on all coal mined and also a rental for the use of improvements and equipment on the property, equal to 7½¢ per ton on all coal mined, which royalty and rental payments were actually paid by Black Gold as sub-lessee direct to Hazard Coal Corporation (R. V, p. 1711; R. IV, p. 1195).

Jeda never had any books and kept no bank account after its organization, all of its accounts and books being handled through Black Gold (R. V, pp. 1711-12; R. IV, pp. 1194-99). In fact after Jeda leased the property to Black Gold there was no further necessity for its existence except to hold the lease from the Hazard Company. Black Gold began operating and shipping coal in January or February, 1931 (R. III, p. 660; R. V, p. 1653). In order to get Black Gold started, Wm. Pendleton and F. A. Garth, employees of Blue Grass, were loaned to Black Gold (R. V, p. 1711; R. III, p. 620; R. IV, pp. 1414-15). It drew upon Blue Grass Mining for cash, taxes, engineering expenses, labor, printing, tramroad and miscellaneous items, aggregating in 1931 \$9,386.64; and borrowed from Blue Grass Mining Company on February 19, 1931, \$1,500.00; February 28, 1931, \$500.00; April 4, 1931, \$300.00; May 9, 1931, \$300.00; May 12, 1931, \$3,000.00 and June 29, 1931, \$200.00, the advancements and loans from Blue Grass Mining Company to Black Gold in that year of its organization \$13,886.64. In 1932, the Kentucky group had Blue Grass Mining Company to lend Black Gold \$2,405.00, and had it to advance it money to pay expenses, labor, engineering, etc., \$3,379.17, and in 1933 had the Blue Grass to lend Black Gold \$500.00 and to advance engineering costs of \$601.80, the aggregate of the funds loaned and labor and money advanced by Blue Grass Mining Company to Black Gold in the years 1931 to 1933, inclusive, being \$22,342.61 (Lav. Ex. X; R. I, p. 400).

The \$10,000.00 borrowed from Hazard Coal Corporation by the organizers of Black Gold was not put into the business until 1931, (R. V, pp. 1708, 1715), after the Company had been started by the use of Blue Grass funds and was shipping coal, and this \$10,000.00 was paid back from the sinking fund of 5¢ per ton on the coal mined.

It was not until April 17, 1931, when Black Gold was then a going concern as the result of the use of Blue Grass money, that the Kentucky group put any money into it whatsoever, at which time, although petitioners insisted below no money was put in by the Kentucky group, the Court found that J. E. Johnson, Sr., put \$5,000.00 into the business. No other money was put in by the Kentucky group or anyone else, other than the \$10,000.00 which was paid back from coal mined (R. I, p. 399).

Black Gold and Jeda Corporations were founded and financed to the operating stage wholly and exclusively by Blue Grass funds and the credit for its foundation enabled it to repay the \$10,000.00 borrowed by its organizers from the sinking fund of 5¢ per ton on coal mined, and further enabled it to pay \$50,000.00 in salaries to members of the Kentucky group and their associate, W. E. Davis. The Court found that Black Gold was not financed wholly by Blue Grass funds, and this may be technically correct in that some money was borrowed by its organizers, but this money was paid back out of coal mined and the mining operations were started and the Company launched upon a successful career wholly by the use of Blue Grass money. This money was subsequently paid back by Black Gold Mining Company to the Blue Grass Mining Company, but not until after the \$10,000.00 which had been borrowed by its organizers and put into the business had been repaid, and then only with interest on a part of it. By reason of this repayment the trial Court held that the Blue Grass Mining

Company had not suffered a loss. However, the record shows that these funds which the Kentucky group loaned to themselves were at all times needed in the business of the Blue Grass Mining Company, and that it suffered by reason of not having this capital in its business in numerous ways, according to the evidence of most of the Kentucky group themselves. Whether it did or did not suffer a loss, however, we submit is not controlling, but the fact that the members of the Kentucky group loaned this money to themselves, from which they made large profits, entitles the Blue Grass Mining Company as a matter of law, to these profits. As said by this Court in *Barney v. Saunders*:

“It is a well-settled principle of equity, that wherever a trustee, or one standing in a fiduciary character, deals with the trust estate for his own personal profit, he shall account to the cestui que trust for all the gain which he has made. If he uses the trust money in speculations, dangerous though profitable, the risk will be his own, but the profit will inure to the cestui que trust. Such a rule, though rigid, is necessary to prevent malversation.”

Barney v. Saunders, 16 Howard 542-3, 14 L. Ed. 1051.

The opinion and decree of the lower courts are probably in conflict with the decisions of this Court in *Barney v. Saunders, supra*, and the following:

Hollins v. Brierfield Coal & I. Co., 150 U. S. 371, 14 Sup. Ct. Rep. 127, 37 L. Ed. 1113.

Twin-Lick Oil Co. v. Marbury, 91 U. S. 587, 23 L. Ed. 328.

Koehler v. Black River Falls Iron Co., 2 Black 715, 17 L. Ed. 339.

Jackson v. Ludeling, 21 Wall. 616, 22 L. Ed. 492.

Wardell v. Union P. R. Co., 103 U. S. 651, 26 L. Ed. 509.

Wright v. Kentucky &c. G. E. R. Co., 117 U. S. 72, 6 Sup. Ct. Rep. 697, 29 L. Ed. 821.

Drury v. Milwaukee &c. S. R. Co., 7 Wall. 299, 19 L. Ed. 40.

See also *Backus v. Finklestein*, *supra*, *Webster Loose Leaf Filing Co.*, 252 Fed. 959. In lending money of the Blue Grass Mining Company to Black Gold Mining Company, the Kentucky group were lending it to themselves. *Geddes v. Anaconda Copper Min. Co.*, 254 U. S. 590, 65 L. Ed. 425; *Highland Cotton Mills v. Rayon Knitting Mills*, 194 N. C. 88, 138 S. E. 431.

The matters involved in this petition, while upon their face appear to be a controversy between private citizens in which it may be argued the public has no interest, nevertheless we respectfully submit that they are charged with a public interest, since the very foundation of society rests upon the principles of common honesty and fair dealing in business matters, and it is a matter of public interest that those occupying a fiduciary relation should be held to the highest and strictest degree of good-faith and fair dealing. We apprehend this may be accomplished by an unbending application of the harsh rules to trustees found to be guilty of wilful misconduct or of fraud in fact. Any relaxation of the high standard set by the courts for the conduct of persons occupying a fiduciary relationship must have an effect reaching far beyond the circle of those immediately involved. It is not enough that unfaithful trustees should be required to restore a part or even all of their illegal gains from the use of the trust property, as this would be an encouragement of such trustees to gamble with trust funds in the belief that if they should be challenged they at least might reap some profit from or recover some compensation for handling the trust estate. Where wilful misconduct, bad-faith and fraudulent breach of trust are established, as

has been in this case, and as was found by the Courts below, the harsh rule should be applied, in our opinion, denying the unfaithful trustees any compensation and stripping them of all gains which they may have made by the use of the trust estate.

We respectfully submit that the language used by the late Mr. Justice Cardozo, then Chief Justice of the New York Court of Appeals, in *Meinhard v. Salmon*, 249 N. Y. 458, 164 N. E. 545, 62 A. L. R. 1, is apropos:

“Many forms of conduct permissible in a workaday world for those acting at arm's length are forbidden to those bound by fiduciary ties. A trustee is held to something stricter than the morals of the market place. Not honesty alone, but the punctilio of an honor the most sensitive, is then the standard of behavior. As to this there has developed a tradition that is unbending and inveterate. Uncompromising rigidity has been the attitude of courts of equity when petitioned to undermine the rule of undivided loyalty by the ‘disintegrating erosion’ of particular exceptions. * * * Only thus has the level of conduct for fiduciaries been kept at a level higher than that trodden by the crowd.”

Respectfully submitted,

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